NRG Energy, Inc.
211 Carnegie Center
Princeton, NJ 08540
Phone: (609) 524-4645
Fax: (609) 524-4941
www.nrgenergy.com

Caroline Angoorly
Vice President & General Counsel, Northeast
caroline.angoorly@nrgenergy.com

August 17, 2006

BY E-MAIL and BY HAND
(bruce.burcat@state.de.us)

Mr. Bruce Burcat
Executive Director
Delaware Public Service Commission
861 Silver Lake Blvd., Suite 100
Dover, DE 19904

Delmarva Power & Light Company's ("DPL") Compliance Filing and Application for Approval of Proposed Request for Proposals ("RFP")

Dear Mr. Burcat:

NRG Energy, Inc. very much appreciates the opportunity to actively participate with the Delaware Public Service Commission ("**PSC**") and other stakeholders in the above matter, commencing with the Public Workshop scheduled for August 18, 2006 to be held at Legislative Hall in Dover (the "**Workshop**").

While we are currently preparing our more detailed comments for submission to the PSC by August 31, 2006, we wanted to outline some of the key issues that we have identified with respect to DPL's proposed RFP to date, to facilitate discussion at the Workshop. We believe that resolution of these issues, described below, will fundamentally influence whether or not the RFP is successful in bringing much-needed new electric generating capacity to Delaware that provides fuel diversity, more stable energy prices for Delaware's citizens, technology innovation and significant environmental benefits.

A. Delaware's Overarching Policy Imperatives

Passage of the Delaware Electric Utility Retail Customer Supply Act of 2006 (the "**EURCSA**") signaled Delaware's adoption of very forward-thinking and explicit policy measures to encourage new baseload generation in the State. In particular, the spirit and intent of the EURCSA is to encourage development of baseload generation in Delaware that utilizes innovative technologies: diversifying away from high and volatile priced gas-fired generation, while materially decreasing emissions of key pollutants and providing real potential for the capture and sequestration of carbon dioxide. To advance these important policy objectives through an effective partnership between the State and the power industry, the RFP should be carefully and consistently crafted to unambiguously reflect, and ensure realization of, these State priorities for the economic and environmental benefit of all Delawareans. We respectfully suggest that the proposed RFP fails to reflect this State policy in a number of material respects.

By way of example for the purposes of this letter, we refer to the Proposal Evaluation mechanics, where it is stipulated that more points will be awarded to bids employing technologies with longer track records of meeting availability requirements, but then also states that DPL "will provide a preference for projects using innovative technology … based on performance guarantees offered by the bidder". This language is fundamentally inconsistent with the policy of encouraging a new set of generation technologies in the State through effective risk-sharing between the participants, given its bias towards technologies with long track records.

As currently drafted, we seriously doubt that the RFP would allow NRG to bid because: (a) the bid size is too small; (b) the terms are not financeable; (c) DPL's criteria for evaluating bids against its own Integrated Resource Planning ("**IRP**") are not transparent and balanced; (d) the required security is unreasonably excessive; and (e) limiting bidders to only investment grade entities effectively bans not only NRG, but virtually all otherwise experienced and qualified bidders. We have elaborated on these issues in the balance of this letter and welcome the opportunity to discuss them with you at tomorrow's Workshop. In addition, we will provide our complete written comments to the PSC by the end of the month. We look forward to working with you on the expedited schedule set to ensure that the final RFP can be optimally effective to attract new generation in Delaware consistent with the EURCSA.

B. Threshold Issues with the RFP

1. Size of the Proposed RFP: The new generation resources sought by DPL must be sized to facilitate achievement of the EURCSA goals. EURCSA is clear in its promotion of projects which offer cost-effective means for achieving power price stability in Delaware. The best way to achieve this objective is to encourage more economically and operationally efficient units. The current 200 MW size of the proposed Power Purchase Agreement ("**PPA**") makes it impossible for DPL, on behalf of the State's consumers, to realize the economies of scale for a baseload generation project – the usual minimum size of such units being 500-600 MW. The 200 MW criterion will effectively exclude bids based on solid fuel generation and particularly those using innovative technologies. It is these technologies that will underpin a significant shift in the electricity industry in Delaware to more efficient and environmentally friendly solid fuel generation, while preserving fuel diversity and minimizing consumer exposure to natural gas supply or price shocks.

2. Financeability: The type of project that will deliver most benefit to Delawareans, consistent with the EURCSA and State policy, is a large, capital intensive and complex undertaking, capable of delivering more than $1 billion of investment in the State, together with many new jobs. The RFP must therefore be structured to provide clear incentive and support to the parties best able to timely and economically bring the necessary generation resources to fruition – through the allocation and management of all related business risks. A key component of this will be securing the necessary project financing.

   Project financing is a particular type of structured funding that is almost always utilized in large infrastructure and energy projects in the US and internationally. Under this approach, lenders provide capital to a special-purpose project entity, and look only to the cash flow generated by the project for payment of all operating expenses as well as debt service – so-called "non-recourse" lending. Achieving such non-recourse status requires that all project contracts, the PPA in particular, be structured to be "financeable". There are a number of parameters contained in the proposed RFP which will make the DPL PPA unfinanceable and therefore discourage bids to provide the new generation resources that Delaware needs. Some examples of these types of provisions include:

a. *Regulatory Out:* The proposed unilateral right of DPL to terminate the PPA at any time during its term if full recovery of all amounts payable under the PPA is not permitted by the PSC. This right creates such fundamental uncertainty in the revenue stream expected from the project that no developer would be willing to commit to the large capital investment needed – and certainly no lender would ever provide financing to such a project – since there would always be a question as to whether the long term revenue stream of the project would be sufficient (in duration and amount) to repay debt and provide a return on equity;
b. *Change-in-Law Exposure:* The lack of protection for each party to the PPA in the event that laws change in future, to preserve the economic deal that is negotiated at the outset;
c. *Early Termination Rights for Permitting:* The proposed period of 18 months for permitting is too short to allow the successful bidder sufficient time to obtain all necessary permits and other governmental approvals required for the project, particularly for more involved projects involving innovative technologies. NRG anticipates a 24-month permitting process and will need some cushion beyond this, in case there are delays; and
d. *Termination Right with Insufficient Compensation:* The PPA provides for DPL to effectively abandon its rights under that contract at any time with the payment of a nominal amount ($50/kW) to the project owner. Projects will not get developed and financed where the risk of termination is not mitigated by receipt of a payment that pays down all outstanding debt and provides a return on equity. For example, a 630 MW Integrated Gasification Combined Cycle ("**IGCC**") project would cost over $1 billion, yet would only trigger a DPL buyout under the PPA as proposed of $31.5 million.

3. Evaluation Criteria: Throughout the RFP, DPL refers to various evaluation criteria, including various models. The main emphasis is upon minimizing the capital cost of any proposed project, implicitly favoring combined cycle gas plants while ignoring the significantly higher operating costs of such plants versus solid fuel generators. This one-dimensional focus on capital cost in the majority of the point weightings, rather than overall value to the system of any proposed project, skews project selection to exactly the type of plants that the EURCSA is mandating a diversification from.

   To achieve the best result for Delaware from the RFP process, all evaluations should employ objective and transparent standards. The use of PJM models and assumptions, as publicly available from time to time, will ensure that any new generation project in Delaware is an optimized resource within the ISO. However, the use of less transparent or publicly available DPL simulations and assumptions as described in the proposed RFP (for example relating to commodity forward price curves, loss under probability of default analyses, bidder price evaluations, imputed debt claims and transmission and distribution impacts), may not in fact select the new generation resources which Delaware needs and which are consistent with the clear policy objectives of the EURCSA. Maximum transparency will allow bidders to tailor their proposed projects and RFP responses to more clearly meet the goals of the State – resulting in a better outcome for its citizens.

4. Required Security: It is customary for PPAs to require certain security from the sellers of power, depending on the applicable stage of development, construction or operation. The security requirements contained in the RFP do not comport with our experience of similar solicitations and

are likely to discourage credible bidders in the Delaware process. During operations, DPL calls for two years of security for capacity and full replacement energy. Using again the above example of a 630 MW IGCC plant, this would equal nearly $500 million. DPL's required security for energy, for example, should be no more than the (negative) differential between the contracted price under the PPA and the market price of any replacement power purchased due to the failure of the project to generate as required.

5. Pool of Bidders: To maximize the quality of the response to the RFP, submissions from the most qualified parties to develop, finance, construct, own and operate the required new generation assets must be encouraged. The proposed RFP contains a number of provisions that run counter to this result, including by effectively disqualifying bidders that are not investment grade. As discussed in Section (B)(2) above on "Financeability", the most common structure for undertaking a new generation project is one that involves a special purpose project entity and project financing. Inherently, such project entities are not rated at all, much less at investment grade. Additionally, the RFP contemplates that DPL may itself be a bidder, including having the benefit of certain exceptions to the bidding requirements (e.g., posting security). Pursuant to Delaware's electricity deregulation laws, DPL and other utilities divested their generation assets, and this RFP ought not to contemplate the participation as a bidder of DPL or other utilities, other than through their respective unregulated affiliates – in which case they should be subject to the same terms and conditions as all other bidders.

Thank you for allowing us to engage with you and the other stakeholders in this critical initiative for Delaware. We look forward to working with you to structure a process that is most likely to yield what Delaware citizens need most: reliable and affordable new generation resources that utilize innovative technologies to contribute to greater energy price stability in the State and enhanced environmental quality.

Yours truly,

Caroline Angoorly

CC: Ms Karen Nickerson (karen.nickerson@state.de.us)
Mr Bob Howatt (robert.howatt@state.de.us)